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Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-1645

TRANSAMERICA MORTGAGE ADVISORS, INC. (TAMA); KENT L. COLWELL; J. WENDELL COOMBS; JOHN R. JENSEN; RALPH D. WENGER; JOHN HAVENS; TRANSAMERICA CORPORATION; TRANSAMERICA LAND CAPITAL, INC.; and MORTGAGE TRUST OF AMERICA,

Petitioners,

—v.—

HARRY LEWIS,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR RESPONDENT

ERIC L. KEISMAN
Attorney for Respondent
845 Third Avenue
New York, New York 10022
(212) 759-4600

Of Counsel:

PHILIP JONES
MARIAN R. PROBST
SAMUEL R. DOLGOW
WOLF POPPER ROSS WOLF & JONES

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—v.—

HARRY LEWIS,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR RESPONDENT

Opinions Below

The opinion of the District Court, incorporated in its order (A. 24-25),[1] and a further order of that Court dismissing the action (A. 26-27), are unreported.

The opinion of the Court of Appeals for the Ninth Circuit (A. 28) is reported at 575 F.2d 237 (9th Cir. 1978).

The majority opinion of the Court of Appeals holds simply that a private right of action for injunctive relief and damages may properly be implied under Section 206 of

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[1] All "A. ....." references are to the Single Appendix.

the Investment Advisers Act of 1940, resting upon the reasoning in the majority opinions in *Abrahamson* v. *Fleschner*, 568 F.2d 862 (2d Cir. 1977), *cert. denied*, 436 U.S. 913 (1978), and *Wilson* v. *First Houston Investment Corp.*, 566 F.2d 1235 (5th Cir. 1978), *petition for cert. docketed*, No. 77-1717. The dissenting opinion adopts the dissent in *Abrahamson* v. *Fleschner*, 568 F.2d at 879.

Jurisdiction

The jurisdictional requisites are adequately set forth in *Brief for Petitioners* at 2.

Question Presented

May a private right of action be implied under the Investment Advisers Act of 1940?

Statutes

The pertinent provisions of the Investment Advisers Act of 1940, 15 U.S.C. § 80b-1, *et seq.*, are Sections 206,[2] 214[3] and 215(b),[4] which are set forth in the Addendum to this Brief.

Statement of the Case

This action was begun by respondent, as a shareholder of MTA, suing derivatively on behalf of MTA and representatively on behalf of its shareholders, in April 1973, in

[2] Aug. 22, 1940, c.686, Title II, § 206, 54 Stat. 852; Sept. 13, 1960, Pub. L. 86-750, §§ 8, 9, 74 Stat. 887.

[3] Aug. 22, 1940, c.686, Title II, § 214, 54 Stat. 856.

[4] Aug. 22, 1940, c.686, Title II, § 215, 54 Stat. 856.

the United States District Court for the Southern District of New York.

The complaint alleges, *inter alia*, violations of Section 206 of the Investment Advisers Act of 1940, 15 U.S.C. § 80b-6, arising out of the making and performance of the investment advisory agreement between petitioners Mortgage Trust of America ("MTA") and Transamerica Mortgage Advisors, Inc. ("TAMA"). (A. 3.)

MTA is a real estate investment trust, organized and operated so as to qualify as such under Sections 856-858 of the Internal Revenue Code of 1954, as amended, 26 U.S.C. §§ 856-858 (1970). Shortly after its organization in 1969, it issued to the public more than 3,168,000 shares of beneficial interest. (A. 4, 5.) MTA was established to invest in a diversified portfolio of real estate mortgages of various types, other real estate loans and some equity interests in real estate; and has transacted business throughout the United States. (*Id.*)

TAMA was, since June 1969, the investment adviser to MTA, pursuant to an advisory agreement first made at or about the time of MTA's organization. (A. 8.) It advises MTA with respect to MTA's investment portfolio and also administers its day-to-day operations. (*Id.*) TAMA, a third-tier subsidiary of petitioner Transamerica Corporation ("Transamerica"), has been MTA's only investment adviser; and MTA has been TAMA's only client. (A. 28.)

Petitioner Transamerica was the parent of TAMA and the sponsor of MTA, and the parent of Transamerica Land Capital, Inc. ("TALC"). MTA acquired about half of its initial investment portfolio from TALC (A. 14), as well as its original officers and employees.

The named individual defendants in the action, including the individual petitioners, were the trustees of MTA;

several of whom, including petitioners Colwell, Coombs, Jensen and Wenger, had at the same time been affiliated as officers with Transamerica, TAMA or other Transamerica subsidiaries. (A. 9.)

The complaint asserted six causes of action; the first three being derivative claims on behalf of MTA, and the latter three being restatements of the former, cast in representative form. (A. 3 *et seq.*)

The first cause of action asserts that fraudulent conduct and practices permeated the making and performance of the advisory agreement between MTA and TAMA; and sought avoidance of that contract or any renewal or extension thereof, as well as restitution of compensation paid thereunder, and consequential damages. (A. 4-14, 20.) Because Transamerica controlled and dominated MTA and TAMA, and exercised that domination with respect to both the formation and performance of the advisory relationship, the complaint charged, MTA was caused to enter into a contract of adhesion with TAMA, the very design of which required that unwarranted, unlawful and grossly excessive fees would be paid by MTA. The making and performance of the advisory contract, as well as the extraction of grossly excessive fees thereunder, are alleged to violate Section 206 of the Investment Advisers Act. (A 10-12.)

The second cause of action asserts fraud and overreaching in the transactions by which MTA purchased its initial investments from TALC. (A. 14-16.) It attacks a course of conduct whereby Transamerica, TAMA and TALC effectively transferred TALC's entire portfolio to a passive MTA, whose trustees allowed the transaction without exercising their own judgment in assessing the investments; and charges that, as a result, MTA received a low-quality portfolio, in a transaction designedly for the benefit of Transamerica, TALC and MTA. (A. 15, 16.)

The third cause of action asserts additional fraudulent and manipulative conduct in the course of performance of the advisory agreement. It charges that, due to the relationship between TAMA and Transamerica, and their dominance and control over MTA, they retained the most desirable opportunities for other Transamerica affiliates, passing on less desirable investments to MTA. Once again, violation of the antifraud provisions of the Advisers Act as well as of the advisory agreements is alleged. (A. 16-18.)

Issue was never joined. Rather, petitioners here moved to dismiss and for summary judgment in March 1974. By that time, the action had been transferred to the Northern District of California. (A. 1.)

Although numerous grounds for dismissal or summary judgment were urged by petitioners, only one was decided by the District Court. It granted the motion to dismiss, saying, "since Section 206 . . . affords no private right of action . . . the Court has no jurisdiction of the plaintiff's claims . . . ." (A. 25.) The holding was not limited to the facts of the particular case. While leave to amend was allowed, plaintiff declined to do so; and a final order of dismissal with prejudice was entered on November 21, 1974. (A. 26.)

Respondent appealed to the Court of Appeals, which reversed. (A. 28 *et seq.*) The majority opinion noted that, "in view of the naked holding of a lack of jurisdiction," the District Court had determined only one issue; and that the Court of Appeals would review that issue only. It then answered affirmatively the question presented for review:

> "Accordingly, we hold that the implication of a private right of action for injunctive relief and damages

> under the Advisers Act in favor of appropriate plaintiffs is necessary to achieve the goals of Congress in enacting the legislation. The District Court holds subject matter jurisdiction to entertain such actions . . . ." (A. 31.)

The Court of Appeals majority opinion explicitly adopts the "rationale of the majorities in *Abrahamson* and *Wilson*." (A. 31.) The dissent, while noting that "reasonable minds may differ," adopted the basis of the dissent in *Abrahamson*. (A. 32.)

Petitioners sought certiorari, proffering the issue, "May a private right of action be implied under the Investment Advisers Act of 1940?" (*Petition for Certiorari* at 2.) The writ was granted on November 6, 1978, without modification of the question presented by the petition. Petitioners now, in their brief, propose that the question for decision is, "May a private right of action *at law for damages* be implied under the Investment Advisers Act of 1940?" (*Brief for Petitioners* at 2; emphasis added.)

Summary of Argument

Each of the Courts of Appeals that have decided the question has held that private rights of action arise by implication under the Investment Advisers ("Advisers Act"), particularly the antifraud provision, Section 206. This is wholly correct in terms of traditional jurisprudence, applicable federal authority and sound policy. The standards established by this Court, as expressed in *Cort* v. *Ash*, 422 U.S. 66 (1975), and in the context of the federal securities laws, have been followed.

Implication of private rights of action under the federal securities laws is not unique. The concept is founded in authority more than a century old.

The propriety of the implied rights recognized by the Courts of Appeals is illuminated by their genesis. Originally, it was held that, where a statute declared conduct unlawful, and violation of the statute caused harm to a person intended to be protected by it, a private action lay, absent a clear legislative intent to deny the right. In diverse contexts, this doctrine was widely utilized by the state courts; and was given the imprimatur of leading commentators.

This Court, with the refinement that the violation must have harmed a member of the "class for whose especial benefit" the statute was intended, applied the doctrine long ago. *Texas & Pacific Ry. Co.* v. *Rigsby*, 241 U.S. 33 (1916). Virtually unchanged in expression and content, it was the core of the first decision to uphold an implied private right of action under the securities laws, *Kardon* v. *National Gypsum Co.*, 69 F. Supp. 512 (E.D. Pa. 1946). This Court and other federal courts have implied private rights under statutes regulating labor relations, telecommunications, navigation and voting rights, as well as the Constitution itself. The present case, and the many decisions implying private rights of action under the securities laws, are thus part of a broader line of authority.

The federal securities laws, including the Advisers Act, are an integrated body of regulatory enactments, serving a common goal: comprehensive national regulation of the securities industry, in order to protect investors; and consequently protecting the capital market and the national economy. The cases upholding Advisers Act claims are supported by the consistent recognition of implied rights of action arising under other securities laws. Section 206 of the Advisers Act is most closely akin to Section 10(b) of the Securities Exchange Act of 1934, and Rule 10b-5 promulgated thereunder; so that the courts have appro-

priately placed significant reliance, in finding implied private rights under Section 206, upon the overwhelming consensus that they were properly implied under Section 10(b) and Rule 10b-5. There is further strong support for such recognition, particularly in the present case, from the parallel contracting-avoiding provisions of the 1934 Act (Section 29(b)) and the Advisers Act (Section 215(b)), which require private action for their effectuation. Such statutes should be held to give rise to the remedies that will fulfill the congressional purpose in enacting them. To deny such rights and remedies under Section 206 of the Advisers Act would create an unjustified anomaly.

Application of each of the four relevant considerations, or criteria, set forth in *Cort* v. *Ash, supra,* points to affirmance of the Court of Appeals here: (1) The statute was enacted for the protection of an especial class, and creates federal rights. (2) There are implicit, if not explicit indications of intention to create such rights; and no indications to the contrary. (3) Implication of private remedies is consistent with the underlying legislative purposes. (4) The cause of action is federal, in an area of particular federal concern, and should be so adjudicated.

Petitioners, as signaled by their unilateral revision of the question on which the Court has granted certiorari, do not squarely meet the issues. Instead, each argument offered for reversal is couched in terms of the alleged absence of support in the statute or its legislative history for implication of a private right of action "at law" for damages. (*E.g., Brief for Petitioners* at 7, 10-21.) This abandonment of a major portion of the question on which certiorari was sought and granted is an effective concession that the decision of the Court of Appeals must be affirmed; and may well call in question whether the writ should not be dismissed. Except for a few scattered, unsupported assertions, petitioners have conceded that it is proper to allow private equitable actions under the Advisers Act. This case is first and foremost a suit in equity, seeking declaratory and injunctive relief, rescission and restitution, on the basis of fraud and overreaching in the making and performance of an investment advisory contract. On other claims, damages are sought, but the primary character of the suit is equitable. Even were there doubt as to "actions at law," this case, as an equitable suit, is maintainable in the federal court, seeking the relief provided by Section 215(b) for violation of Section 206 of the Advisers Act.

(1) The statute was enacted for the especial benefit of investors in the context of their contractual relationships and other transactions with investment advisers; which is manifested by its regulatory and antifraud provisions and by Congress' articulated fundamental purpose: to protect investors from fraud and misrepresentation by unscrupulous advisers. The first question posed in *Cort* v. *Ash,* 422 U.S. 66 (1975), must be affirmatively answered. A federal right is created by the statute.

(2) The explicit or implicit indication of legislative intent, which favors implication of private rights of action, is in the Advisers Act *per se,* and the unambiguous declarations of its purpose. Sections 206 and 215(b), properly interpreted, indicate implicit intent favoring implication of a private right of action. The primary and legitimate sources of legislative history are silent on the subject of private actions, and barely descriptive of the pertinent provisions. The essential purpose of the statute is, however, firmly, even bluntly, stated; and the secondary sources relied on by petitioners as diluting or negating that purpose are either silent or utterly beside the point; or support respondent's position. Given the

text and purpose of the relevant provisions, the courts should make available remedies to protect the rights created.

Absence of the phrase "actions at law" from Section 214 of the Advisers Act neither excludes jurisdiction over private actions nor manifests an intention to preclude them. Section 214 was so described, in all legislative materials, as to require the conclusion that Congress did not perceive it as differing, in any material aspect, from the congruent provision of the Investment Company Act, which, like the earlier securities statutes, did contain the phrase. Section 214 has virtually no legislative history of its own; and what there is explains nothing. There is no warrant in Section 214 for dilution of the substance of the antifraud section or for nullification of the rights obviously embodied in Section 215(b). Section 214 does not manifest any purpose of Congress to disallow recognition of the implied rights that will provide effective recourse for violations of the Advisers Act.

Proper application of the second of the *Cort* v. *Ash* criteria also favors recognition of implied rights of action, to vindicate the legislative purpose of the statute.

(3) Similarly, implication of private rights of action is consistent with the underlying purpose of the legislative scheme. That underlying purpose is the already-described fundamental purpose. There is no conflict between the central thrust of the regulatory scheme and any co-existing or subsidiary aims. Such inconsistency has been found only where the statute involved created no federal right in the plaintiff, or where recognition of a private claim would interfere with a comprehensive legislative scheme for administrative enforcement.

Agency enforcement of the Advisers Act, like the other securities laws, is complemented, not hampered, by the exercise of private rights. Thus, once the first two relevant criteria are satisfied, it should follow that the third is met. In the proper sense, private actions are necessary to enforcement; since the Securities and Exchange Commission cannot alone enforce the statute so as fully to protect investor interests.

(4) Protection of investors, *vis-a-vis* investment advisers, is a federal concern. The Advisers Act creates federal rights in them. Federal courts should vindicate those rights. It is no answer that there may exist analogous state law causes of action. This is true of most cases where implied federal rights have been recognized. Analogous state law claims are recognized to be ill-adapted or simply inadequate. Uniform federal law should provide the substantive context of federally created rights. The fourth of the *Cort* v. *Ash* questions should be answered in the negative.

That this Court has defined and limited certain rights arising under the securities laws is not precedent for reading the Advisers Act to confer no rights. The suggestions of excessive and ill-founded litigation, made as petitioners' "practical" policy argument, are unsupportable chimera, and the asserted facts and characterizations offered in support are significantly false—in addition to being outside the record.

The federal courts are, and should continue to be, a forum for the proper interpretation and application of federal law, especially in fields of national concern. The regulation of the securities industry is one such field. That is the controlling policy consideration. The decision of the Court of Appeals should be affirmed.

ARGUMENT

I.

Implication of Private Rights of Action Under Section 206 of the Advisers Act Is Called for by Consistent Application of Precedent in General Federal and Common Law Jurisprudence.

Each of the three Courts of Appeals that has recognized the propriety of an implied private action for equitable relief and for damages as arising under Section 206 of the Investment Advisers Act of 1940, in the case at bar, in *Abrahamson* v. *Fleschner,* 568 F.2d 862 (2d Cir. 1977), *cert. denied,* 436 U.S. 913 (1978), and in *Wilson* v. *First Houston Investment Corp.,* 566 F.2d 1235 (5th Cir. 1978), has built upon the prior decisions of this Court upholding the implication of such claims under comparable statutes, and other federal authority in securities and related areas of law. These lines of authority arise, in turn, from firmly rooted concepts in Anglo-American jurisprudence.

Further, these Courts have carefully adhered to the standards established in *J. I. Case Co.* v. *Borak,* 377 U.S. 426 (1964), and *Cort* v. *Ash,* 422 U.S. 66 (1975). Recognition of an implied right of action under Section 206, is conceptually no more novel than recognition of such rights under antifraud and similar provisions of the related federal securities laws. Review of the origins and development of the underlying principles should guide their application here.

The fundamental concept is that, where the legislature has declared certain conduct unlawful, and where the proscribed conduct is recognized as invading particular rights of a discrete group, or class, of persons, as well as the

sovereign interest, it is appropriate that an action should lie on behalf of an injured member of that class. The principle was clearly articulated more than a century ago by Lord Campbell, in *Couch* v. *Steel,* 3 E. & B. 402, 118 Eng. Rep. 1193 (Q.B. 1854). It was held there that an action on the case lay in favor of a seaman who claimed damages for illness arising from his shipowner's failure, in violation of a penal statute, to maintain certain medicines on board a vessel. Only the count based on the statutory violation was sustained against a demurrer. The Court based its holding on sources still more ancient, saying:

> "The enactment provides a benefit for the seamen; and, according to the plaintiff's allegations in the second count, the defendant has violated this enactment; and thereby the plaintiff, being a seaman on board, was deprived of that benefit, and his health was injured. The general rule is that, 'where a man has a temporal loss, or damage by the wrong of another, he may have an action upon the case, to be repaired in damages;' Com. Dig. Action upon the Case (A). The statute of Westm. 2 (1 stat. 13 Ed. 1,) c. 50, gives a remedy by action on the case to all who are aggrieved by the neglect of any duty created by statute. See 2d. Inst. 486. And in Com. Dig., Action upon Statute (F), it is laid down that, 'in every case, where a statute enacts, or prohibits a thing for the benefit of a person, he shall have a remedy upon the same statute for the thing enacted for his advantage, or for the recompence of a wrong done to him contrary to the said law.' Therefore the simple enactment requiring the supply of medicines would have entitled the plaintiff to an action, in the same manner as if the obligation had been imposed by the common law, or had been expressly included in the ship's articles." (3 E. & B. at 411.)

Rejecting the argument that provision of a monetary penalty (recoverable by an informer) had been intended to exclude the right of recovery by the party injured, the Court held that absent statutory language explicitly denying the right, a breach of statutory duty causing special damage to an individual plaintiff, beyond the public wrong, gave rise to an action on the case.

The law thus stated was generally accepted in this country. *See* Thayer, *Public Wrong and Private Action*, 27 Harv. L. Rev. 317 (1914); 5 Loss, *Securities Regulation* 2883-2886 (Supp. 1969). Dean Thayer was clear that, at least in the case of prohibitory statutes, the rule enunciated should apply with few, if any, exceptions:

> "When such a prohibition has been violated and the very evil aimed at by the law has been brought about, approval of the wrongdoer's conduct by the court is not consistent with proper respect for another branch of the government." (27 Harv. L. Rev. at 324.)

The language of *Couch* v. *Steel, supra,* was echoed where implication of a private action in tort was squarely upheld by this Court, in *Texas & Pacific Ry. Co.* v. *Rigsby,* 241 U.S. 33 (1916), and again in the seminal finding that an implied private right of action arose from an antifraud provisior of one of the federal securities laws, *Kardon* v. *National Gypsum Co.,* 69 F. Supp. 512 (E.D. Pa. 1946).

In the *Rigsby* case, this Court implied a right in favor of a railroad yard employee, not directly engaged in interstate commerce, to recover for damages for personal injuries arising from violation of a provision of the Federal Safety Appliance Acts[5] requiring maintenance of certain railway car equipment in secure and safe condition. It

[5] *E.g.,* 36 Stat. at L. 298, Comp. Stat. 1913, § 8617.

found that the statute was "intended for the *especial protection* of employees engaged in duties" such as plaintiffs' (241 U.S. at 37; emphasis added). While the statutes contained no express language creating a private right of action for personal injury by an employee, there was an analogous common law right of action. In language strikingly similar to Lord Campbell's, the Court said:

> "A disregard of the command of the statute is a wrongful act, and where it results in damage to one of the class for whose especial benefit the statute was enacted, the right to recover the damages from the party in default is implied, according to a doctrine of the common law expressed in 1 Com. Dig., tit., Action upon Statute (F), in these words: 'So, in every case, where a statute enacts or prohibits a thing for the benefit of a person, he shall have a remedy upon the same statute for the thing enacted for his advantage, or for his recompense of a wrong done to him contrary to the said law.' [Citation omitted.] This is but an application of the maxim, *Ubi jus ibi remedium.*" (*Id.,* at 39-40.)

In *Kardon* v. *National Gypsum Co., supra,* whether there was personal jurisdiction over certain defendants depended upon whether a private right of action arose by implication under Section 10(b) of the Securities Exchange Act of 1934[6] ("the 1934 Act"), and Rule 10b-5[7] promulgated thereunder. The Court found that the complaint charged acts violating the statute and rule; and that no statute or rule expressly provided a private action for such violation. Judge Kirkpatrick continued:

[6] 15 U.S.C. 78j(b) (1971).

[7] 17 C.F.R. § 240.10b-5.

"However, 'The violation of a legislative enactment by doing a prohibited act, or by failing to do a required act, makes the actor liable for an invasion of an interest of another if; (a) the intent of the enactment is exclusively or in part to protect an interest of the other as an individual; and (b) the interest invaded is one which the enactment is intended to protect. * * *' Restatement, Torts, Vol. 2, Sec. 286. This rule is more than merely a canon of statutory interpretation. The disregard of the command of a statute is a wrongful act and a tort. As was said in Texas & Pacific R. Co. v. Rigsby, 241 U.S. 33, 39, 36 S. Ct. 482, 484, 60 L. Ed. 874, 'This is but an application of the maxim, Ubi jus ibi remedium.'" (69 F.Supp. at 513.)

Foreshadowing later decisions of both the Courts of Appeals and this Court, Judge Kirkpatrick also considered whether an explicit intention to grant or deny such a remedy could be found in the statute itself, or in the general legislative scheme; rejected the argument that the creation of certain express private rights negatived the implication of others; and found implication of a private remedy appropriate "in view of the general purpose of the Act." (*Id.* at 514).

Adoption of the statutory tort principle in the Restatement of Torts, § 286 (1934),[8] reflecting its widespread acceptance, of course facilitated its application in *Kardon*, and its progeny. Implied rights were found in varying contexts. *See, e.g., Abounader* v. *Strohmeyer & Arpe Co.*, 243 N.Y. 458, 154 N.E. 309 (1926) (food labeling); *H.*

[8] In the Restatement of Torts, 2d, § 286, the formulation of the principle is modified, and stated more flexibly. *See generally* 2 Loss, *Securities Regulation* 935-936 (2d ed. 1961); 5 Loss, *op. cit.*, 2886 (Supp. 1969).

Christiansen and Son Inc. v. *City of Duluth*, 225 Minn. 475, 31 N.W.2d 270 (1948) (obstruction of waterway); *Sapiro* v. *Frisbie, et al.*, 93 Cal. App. 299, 270 Pac. 280 (D. Ct. App. 1928) (zoning violation); *Wolf* v. *Smith*, 149 Ala. 457, 42 So. 824, 9 L.R.A. (N.S.) 338 (1906) (personal injury).

There is no lack of federal authority upholding the implication of private rights of action where the statute in question had been enacted for the benefit of a particular class, and where Congress had not evidenced a purpose to exclude such relief. In *Tunstall* v. *Brotherhood of Locomotive Firemen and Enginemen*, 323 U.S. 210 (1944), this Court, by Mr. Chief Justice Stone, held that petitioner, a Negro fireman, could bring an action for injunctive relief and damages for the failure of the respondent union to represent him "without discrimination because of race," a duty imposed upon the union under the Railway Labor Act (45 U.S.C. § 151 *et seq.*). The Court held that petitioner's claim arose under the statutes of the United States, so that general federal question jurisdiction existed under the predecessor to 28 U.S.C. § 1331. It continued:

"We also hold that the right asserted by petitioner which is derived from the duty imposed by the Railway Labor Act on the Brotherhood, as bargaining representative, is a federal right implied from the statute and the policy which it has adopted. It is the federal statute which condemns as unlawful the Brotherhood's conduct. 'The extent and nature of the legal consequences of this condemnation though left by the statute to judicial determination, are nevertheless to be derived from it and the federal policy which it has adopted.'" (323 U.S. at 213, citations omitted.)

Similarly, the Court of Appeals for the Second Circuit found that a private right of action for damages arose by implication from Section 605 of the Communications Act of 1934 (47 U.S.C. § 151 *et seq.*). In *Reitmeister* v. *Reitmeister*, 162 F.2d 691 (2d Cir. 1947), Judge Learned Hand said:

> "The first questions are whether the Communications Act of 1934 . . . imposes a civil, as well as a criminal, liability upon anyone who 'publishes' a telephone message, and whether, if so, the District Court had jurisdiction over the action. *Although the Act does not expressly create any civil liability, we can see no reason why the situation is not within the doctrine which, in the absence of contrary implications,* construes a criminal statute, enacted for the protection of a specified class, *as creating a civil right in members of the class, although the only express sanctions are criminal. . . . That the District Court had jurisdiction, if there was a civil right, is too plain for debate.*" (162 F.2d at 694; footnotes omitted; emphasis added.)

More recent decisions reconfirm the viability of the doctrine. *Wyandotte Transportation Co.* v. *United States*, 389 U.S. 191 (1967), held that the United States had an implied right of action for damages under Section 15 of the Rivers and Harbors Act of 1899 (33 U.S.C. § 409) against a shipowner who had negligently permitted his vessel to be sunk in a navigable waterway, notwithstanding the existence of explicit criminal penalties for violation of that section, and notwithstanding the existence of explicit civil remedies for violations of other sections of the Act.[9] In *Allen* v. *State Board of Elections*, 393 U.S. 544 (1969), the Court held that there was an implied right of action under Section 5 of the Voting Rights Act of 1965 (42 U.S.C. § 1973 *et seq.*), enabling a private citizen to seek declaratory judgment that a state had violated Section 5 in enacting new voting statutes, as well as injunctive relief against enforcement of the state statutes. The Court emphasized the broad purposes of the Act to assure voting rights to all citizens and the ineffectiveness of enforcement by the federal government alone, and reiterated:

> "We have previously held that a federal statute passed to protect a class of citizens, although not specifically authorizing members of the protected class to institute suit, nevertheless implied a private right of action." (*Id.* at 557.)

Still more recently, in *Bivens* v. *Six Unknown Named Agents of Federal Bureau of Narcotics*, 403 U.S. 388 (1971), this Court implied a private right of action for damages in favor of plaintiffs who alleged injury arising out of an unlawful search and arrest, in violation of rights guaranteed by the Fourth Amendment to the Constitution.

The many cases upholding private rights of action implied from provisions of the federal securities laws therefore lie well within the mainstream of a broader current of authority.

[9] The authority relied on included, *inter alia*, *Texas & Pacific Ry. Co.* v. *Rigsby*, *supra*, *J. I. Case Co.* v. *Borak*, 377 U.S. 426 (1964), and the Restatement (Second) of Torts, § 286.

II.

Consistent Recognition of Implied Private Rights of Action Under Related Federal Securities Laws Militates Strongly for Recognition of Such a Right of Action Under Section 206 of the Advisers Act.

Quite aptly, the Courts in *Abrahamson* v. *Fleschner*, 568 F.2d 862 (2d Cir. 1977), *cert. denied*, 436 U.S. 913 (1978), and *Wilson* v. *First Houston Investment Corp.*, 566 F.2d 1235 (5th Cir. 1978), as well as in the case at bar, drew substantial support for their holdings from the consistent recognition of implied rights of action on behalf of the protected class of investors under Section 10(b) of the 1934 Act and Rule 10b-5, Section 14(a) of the 1934 Act,[10] the Investment Company Act of 1940[11] ("Investment Company Act") and the Public Utility Holding Company Act of 1935.[12] (*See* 568 F.2d at 873.)

There is an unmistakably close correspondence between Section 206[13] of the Advisers Act and Section 10(b) of the 1934 Act and Rule 10b-5.[14] The existence and propriety

[10] 15 U.S.C. § 78n(a) (1971).

[11] 15 U.S.C. § 80a-1 *et seq.* (1971).

[12] 15 U.S.C. § 79 *et seq.* (1971).

[13] Section 206, in pertinent part, declares it unlawful for an investment adviser,

"(1) to employ any device, scheme or artifice to defraud, any client or prospective client;

"(2) to engage in any transaction, practice or course of business which operates as a fraud or deceit upon any client or prospective client;

• • •

"(4) to engage in any act, practice or course of business which is fraudulent, deceptive or manipulative. . . ."

[14] Rule 10b-5, in pertinent part, declares it unlawful,

"(1) to employ any device, scheme or artifice to defraud,

• • •

of implied private rights of action for damages, as well as for injunctive relief, under the latter provisions, are too well settled to require extensive discussion. As this Court noted in *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723 (1975):

> "This Court had no occasion to deal with the subject until 25 years later, and at that time we confirmed with virtually no discussion the overwhelming consensus of the District Courts and Courts of Appeals that such a cause of action did exist. . . . Such a conclusion was, of course, entirely consistent with the Court's recognition in J. I. Case Co. v. Borak . . . that private enforcement of Commission rules may '[provide] a necessary supplement to Commission action.'" (*Id.* at 730.)

It is instructive that the determinations that contributed most strongly to that "overwhelming consensus" relied upon traditional doctrine. For example, in *Fischman* v. *Raytheon Mfg. Co.*, 188 F.2d 783 (2d Cir. 1951), the Court wrote:

> "Section 10(b), to be sure, does not explicitly authorize a civil remedy. Since, however, it does make 'unlawful' the conduct it describes, it creates such a remedy." (*Id.* at 787; footnote omitted.)

Important support for this view arises from Section 29(b) of the 1934 Act,[15] which, like Section 215(b) of the Advisers Act, "provides that contracts in violation of any provision of the Act shall be void." *Kardon* v. *National*

"(3) to engage in any act, practice or course of conduct which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security."

[15] 15 U.S.C. § 78cc (1971).

Gypsum Co., 69 F. Supp. 512, 514 (E.D. Pa. 1946). Judge Kirkpatrick reasoned that:

> "It seems to me that a statutory enactment that a contract of a certain kind shall be void almost necessarily implies a remedy in respect of it. The statute would be of little value unless a party to the contract could apply to the Courts to relieve himself of obligations under it or to escape its consequences." (*Id.*)

The Courts of Appeals that upheld the implication of private rights of action under the Investment Company Act had no greater difficulty. In *Moses* v. *Burgin*, 445 F.2d 369 (1st Cir.), *cert. denied*, 404 U.S. 994 (1971), the Court noted that defendants hardly disputed that the Investment Company Act "impliedly authorizes the courts to grant civil recovery if their conduct fell within the scope of the phrase 'gross misconduct or gross abuse of trust' contained in Section 36 of the Act, 15 U.S.C. § 80a-35." (*Id.* at 373.) The Court considered the implication appropriate, upon its own findings of an apparent legislative purpose to protect shareholders of investment trusts against self-dealing by those who managed the funds; of the utility of private actions as a supplement to SEC activity; and of the "general grant of jurisdiction to 'enforce any liability or duty created by' the Act." (*Id.*) *See also Brown* v. *Bullock*, 194 F. Supp. 207 (S.D.N.Y. 1961), *aff'd en banc*, 294 F.2d 415 (2d Cir., 1961); *Taussig* v. *Wellington Fund, Inc.*, 313 F.2d 472 (3d Cir.), *cert. denied*, 374 U.S. 806 (1963); *Esplin* v. *Hirschi*, 402 F.2d 94 (10th Cir. 1968), *cert. denied*, 394 U.S. 928 (1969); *Herpich* v. *Wallace*, 430 F.2d 792 (5th Cir. 1970).

This Court first upheld an implied private right of action under the securities laws in *J. I. Case Co.* v. *Borak*, 377 U.S. 426 (1964). It determined that Section 14(a) of the

1934 Act, regulating proxy solicitations, was enacted to prevent the obtainment of "authorization for corporate action by means of deceptive or inadequate disclosure" and that the beneficiaries of these "broad remedial purposes" were principally the group of investors who were the stockholders of the subject corporation. *Id.* at 431, 432, respectively. It was equally plain to the Court that the Securities and Exchange Commission could not enforce this provision alone and thus that "[p]rivate enforcement of the proxy rules provides a necessary supplement to Commission action". (*Id.*). The Court said:

> "We, therefore, believe that under the circumstances here it is the duty of the courts to be alert to provide such remedies as are necessary to make effective the congressional purpose." (377 U.S. at 433.)

The federal securities laws, including the Advisers Act, are an integrated body of legislation, constituting a comprehensive regulatory scheme intended by Congress to eliminate a variety of "abuses in the securities industry." *Securities and Exchange Commission* v. *Capital Gains Research Bureau, Inc.*, 375 U.S. 180 at 186 (1963); *Abrahamson* v. *Fleschner*, 586 F.2d 862 (2d Cir. 1977), *cert. denied*, 436 U.S. 913 (1978). The settled propriety of implied private rights of action under the provisions of these laws aimed at elimination of fraud, deception and similar overreaching is a strong basis for implying private rights under Section 206. To hold otherwise would be to create an unjustifiable anomaly.

The standards established by this Court for recognition of implied private rights of action are satisfied here. In *Cort* v. *Ash*, 422 U.S. 66 (1975), four relevant considerations were articulated:

> "First, is the plaintiff 'one of the class for whose *especial* benefit the statute was enacted,' Texas & Pacific

R. Co. v. Rigsby, . . . (emphasis supplied)—that is, does the statute create a federal right in favor of the plaintiff? Second, is there any indication of legislative intent, explicit or implicit, ether to create such a remedy or to deny one? . . . Third, is it consistent with the underlying purposes of the legislative scheme to imply such a remedy for the plaintiff? . . . And finally, is the cause of action one traditionally relegated to state law, in an area basically the concern of the States, so that it would be inappropriate to infer a cause of action based solely on federal law?" (422 U.S. at 78; citations omitted.)

Although these four considerations are interdependent, it will be useful to discuss them separately.

III.

The Protection of Investors in Their Relationships With Investment Advisers Was a Fundamental Purpose of the Advisers Act. The Statute Is for Their Special Protection, and Creates Federal Rights in Their Favor.

The Advisers Act was passed out of a well-founded and particularized concern for the protection of investors in the context of their dealings and agreements with investment advisers. *Securities and Exchange Commission* v. *Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 186 (1963); *see also Abrahamson* v. *Fleschner, supra; Wilson* v. *First Houston Investment Corp., supra; Bolger* v. *Laventhol, Krekstein, Horwath & Horwath*, 381 F. Supp. 260 (S.D.N.Y. 1974); *Sullivan* v. *Chase Investment Services of Boston Inc.*, 434 F. Supp. 171 (N.D. Cal. 1977); *Angelakis* v. *Churchill Management Corp.*, CCH Fed. Sec. L. Rep. ¶ 95,285 (N.D. Cal. 1975).

Full and consistent support for this finding arises from the genesis and legislative history, as well as the provisions, of the statute.

The Advisers Act, like the Investment Company Act, has its roots in a study made by the Securities and Exchange Commission at the direction of Congress.[16] The SEC Report showed that the abuses of investors' interests "prevalent among investment companies" were by no means foreign to the investment advisory business. Particularly, it pointed to dangers presented by advisers "who indulged in exaggerated claims"; by conflicts of interest between investment advisers and their clients; by conflicts, self-dealing and similar problems arising out of affiliations between investment advisers and those who marketed securities to investors; and by the existence of compensation arrangements, including contingent compensation arrangements, which encouraged the adviser to recommend investments involving untoward risks. (SEC Report at 28-30.)

The "declaration of policy," embodied in Section 202 of the bill as originally introduced,[17] recited its recognition of an adverse effect on the interest of investors:

> ". . . (4) When the business of investment advisers is so conducted as to defraud or mislead investors, or to enable such advisers to relieve themselves of their fiduciary obligations to their clients."

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[16] Investment Trusts and Investment Companies, Report of the Securities and Exchange Commission, pursuant to Section 30 of the Public Utility Holding Company Act of 1935, on investment counsel, investment management, investment supervisory and investment advisory services, H.R. Doc. No. 477, 76th Cong., 2d Sess. (1939), hereinafter "SEC Report."

[17] S. 3580, 76th Cong., 3d Sess. (1940).

The intent of the legislation was "to mitigate, and, so far as is presently practicable to eliminate the abuses enumerated. . . ." (*Id.*) While this text was not in the Advisers Act as finally enacted, it remains an accurate description of its fundamental purpose.[18]

The point is stated with equal force in the reports of the Senate and House committees that accompanied the ultimate version of the Act. The report of the Senate Committee on Banking and Currency declared that federal legislation was necessary, in that "protection of investors requires the regulation of investment advisers on a national scale," so as to solve "the problems and abuses of investment advisory services. . . ." (S. Rep. No. 1775, 76th Cong., 3d Sess. 21 (1940).)

The House Committee on Interstate and Foreign Commerce emphasized in its report the need "to protect the public from the frauds and misrepresentations" of dishonest advisers and also to protect honest investment advisers against unwarranted stigmatization "by making fraudulent practices by investment advisers unlawful." (H.R. Rep. No. 2639, 76th Cong., 3d Sess. 28 (1940).)

In the face of this legislative history, petitioners concede that a basic purpose of the Act is "to protect investors who retain investment advisers." (*Brief for Petitioners* at 12.) This correct concession, we submit, is an admission that the first criterion of *Cort* v. *Ash*, 422 U.S. 66, 78 (1975), is met. Petitioners attempt to avoid

[18] As this Court said in *SEC* v. *Capital Gains Research Bureau, supra*, the language was deleted, without altering the substance of the Act, upon the protestations of industry witnesses that all investment advisers should not be publicly condemned for the acts of some; and not because of any congressional doubt that abuses had occurred in the past or that their mitigation or elimination required federal legislation. (375 U.S. at 191 n. 34.)

its force by suggesting that the inquiry should be whether Congress intended especially to benefit investors "seeking money damages for violation of the Act." (*Brief for Petitioners*, at 11, 14.) But in *Cort*, as in all of the authorities, the "class" is unmistakably defined in terms of its pre-litigation or non-litigation characteristics, and in terms of the effects, or potental effects, of the prohibited conduct upon it; not by the way in which redress is sought. *See, e.g., J. I. Case Co.* v. *Borak*, 377 U.S. 426, 432 (1964).

Another pointless evasive tactic is the suggestion that the basic purpose is somehow diluted by the co-existence of other purposes. (*See Brief for Petitioners*, 15-16; 22-23.)

The federal securities laws are avowedly multi-purpose statutes.[19] Their enactment was motivated by the realization that the structure and practices of the securities industry had contributed substantially to the causes of the great depression; and that a regulated, orderly and better behaved capital market was a prerequisite to a healthy national economy. *See, e.g., Securities and Exchange Commission* v. *Capital Gains Research Bureau, supra*, 375 U.S. at 186. It has never been suggested that a statute—or the particular provision of a statute in question—is for the protection of "an especial class" only where that is its *sole* purpose. *Cort.* v. *Ash* itself holds that corporate stockholders are not especially protected by the statute at issue because the statute was concerned with them peripherally if at all; being primarily directed at a very different area of concern: the need to limit the influence of concentrated corporate financial power upon the in-

[19] For example, Section 2 of the 1934 Act declares its purposes to include protection of the "national credit," the taxing power and the "national banking system," as well as the "maintenance of fair and honest markets" in securities transactions. 15 U.S.C. § 78b (1971).

tegrity of the electoral process. (422 U.S. at 82.) In *Texas & Pacific Ry. Co.* v. *Rigsby*, 241 U.S. 33 (1916), the source of the "especial benefit" rubric, protection of travelers and assurance of "the safety of the main track as a highway of interstate commerce," were as significant among the purposes of the statute as the safety of employees. (241 U.S. at 41.) That plaintiff was a member of *one* of the groups especially protected was quite enough.

Section 206, prohibiting fraudulent or deceptive practices, was a part of the Advisers Act from the first draft onward; as was a provision (enacted as Section 215(b)) voiding contracts made or performed in violation of the Act. *Securities and Exchange Commission* v. *Capital Gains Research Bureau, supra.* The desirability of these provisions was never debated, and was presumed by all parties.

It is therefore immaterial that, in some provisions of the Act, the powers granted the SEC were less sweeping than originally proposed. That the Act may have had the additional purpose to cause a compulsory census of the industry—which is a dubious interpretation of early legislative history—is hardly in derogation of its explicit, fully articulated, primary purpose—the protection of investors in the context of their dealings and relations with investment advisers. (See Point IV A, *infra,* p. 30.)

The instant case is brought on behalf of a party within the especially protected group, as were the other actions where a private right of action under Section 206 has been recognized. This case is essentially derivative,[20] and the claims asserted are those of MTA. As is undisputed, MTA is an investor in a contractual relationship with its adviser. It is alleged that the making and performance of the advisory contract involved conduct in violation of Section 206; that the contract itself was unilaterally imposed upon MTA by respondent, due to, and through the exercise of, their control and domination of MTA and its trustees; and that by design the provisions for computation of the advisory fees paid and to be paid under the contract were fraudulent, deceptive and grossly unfair (A. 8-11). Further, it is alleged that a manipulative course of conduct pervaded the relationship. Because of the control of MTA by its sponsor (Transamerica), which also controlled its adviser (TAMA), it is charged that MTA, to its disadvantage, acquired much of its initial investment portfolio from a corporation (TALC) having a comomn parent with its adviser (A. 14). It is also charged that, in the performance of the contract, MTA was harmed in its interest as an investor due to the conflict of interests arising out of the TAMA-Transamerica relationship, in that the best available investments were not offered to MTA (A 17). The abuses asserted here are of the very type that the SEC Report, *supra,* particularly noted; and that the Advisers Act renders unlawful. *Cf. Schoenbaum* v. *Firstbrook,* 405 F.2d 215 (2d Cir. 1968), *cert. denied,* 395 U.S. 906 (1969). *Accord, Superintendent of Insurance* v. *Bankers Life & Casualty Co.,* 404 U.S. 6 (1971).

In *Wilson* v. *First Houston Investment Corp.,* 566 F.2d 1235 (5th Cir. 1978), and in *Abrahamson* v. *Fleschner,* 568 F. 2d 862 (2d Cir. 1977), *cert. denied,* 436 U.S. 913 (1978), plaintiffs were investors who had committed funds to the management of investment advisers, and each charged fraudulent concealment and misrepresentation with respect to the advisers' investment management policies and practices; clearly the sort of abuses at which the Advisers Act was aimed.

Thus, the Courts of Appeals that have held that these plaintiffs met the first criterion established in *Cort* v. *Ash*

[20] While class claims were originally asserted, class determination was never sought (A. 1).

were correct. Its content has not changed since it was first articulated. *See, e.g., Piper* v. *Chris-Craft Industries Inc.*, 430 U.S. 1 (1977). Proper application of this criterion requires the conclusion that Section 206 of the Advisers Act creates a federal right in favor of investors, with respect to their dealings with investment advisers; and thus in favor of MTA.

IV.

There Is at Least Implicit Indication That Some Private Rights of Action Were Intended to Be Allowed Under the Advisers Act. There Is No Indication to the Contrary.

The second criterion in *Cort* v. *Ash*, 422 U.S. 66, 78, is whether there is any explicit or implicit indication of legislative intent to create or deny a private remedy. When, as here, the "especial benefit" criterion is met, it is not necessary to "show an intention" to create a private cause of action" in order properly to imply one; but rather to show the absence of "an explicit purpose to deny such cause of action." (*Id.* at 82.)

A. *Explicit or Implicit Indication of Intent to Create Private Remedies Can and Should Be Found in the Statute Itself and Its Stated Purposes; the Legislative History Being Virtually Silent.*

Apart from such inferences as are validly drawn from the regulatory content of the statute itself, and from its articulated primary purpose, there is no evidence that Congress ever considered "the problem of private actions under the Advisers Act at the time of its enactment." *Abrahamson* v. *Fleschner*, 568 F.2d 862, 874 (2d Cir. 1977), *cert. denied*, 436 U.S. 913 (1978). No section of the statute declares that there shall be private actions, nor does any

section declare that there shall not. Were it otherwise, the question now before the Court could not arise. It is the fact that the primary sources of legislative intention —the conscious expressions of Congress in the cognizant committees—neither discuss nor mention the issue.

A strong indication of at least implicit intention to allow private rights of action under the Advisers Act lies in the nature and purpose of Section 206 *per se*, when it is read, as it should be, in conjunction with Section 215(b) (*see* pp. 40-41, *infra*); and in the light of the paucity of specific legislative history on which to rely. It is beyond dispute—and has been effectively conceded—that there is clear evidence of the propriety of an implied (if not explicit) private equitable claim; and, again, this is dispositive of the present action. Since the argument has been made, however, that an intention to exclude private rights of action can be gleaned from legislative materials (*Brief for Petitioners* at 14-21), analysis and response are required.

The first and best sources of legislative history are the House Report and Senate Report that accompanied the legislation to the floor of Congress. *United States* v. *International Union, UAW-CIO*, 352 U.S. 567, 585 (1957); *American Airlines, Inc.* v. *Civil Aeronautics Board*, 365 F.2d 939, 949 (D.C. Cir. 1966). These represent the prevailing views of those most responsible for the legislation, and are the documents—perhaps the only ones—that can fairly be presumed to have been considered by Congress as a whole.

Each of these reports is simple, terse, descriptive and unenlightening as to the precise issue here.[21] In each, the

[21] In reporting jointly the two proposed statutes, each report devotes the great preponderance of its text to the Investment Company Act (Title I of the bill presented), and rather limited attention to the Advisers Act (Title II of that bill). The House Re-

only section of the Advisers Act having any bearing on the issues here receiving individual mention is Section 206.

The House Report regarding Section 206 says:

> "This section makes unlawful transactions and practices by investment advisers which defraud or operate as a fraud or deceit upon clients or prospective clients." (H.R. Rep. No. 2639, 76th Cong., 3d Sess. 30 (1940).)

The Senate Report says:

> "Transactions and practices which defraud or operate as a fraud or deceit upon clients or prospective clients are prohibited." (S. Rep. No. 1775, 76th Cong., 3d Sess. 22 (1940).)

There is no separate discussion in either the House Report or the Senate Report of any other provision of the Act which may bear upon the question before this Court. As to Section 214, the keystone of the argument for reversal, the substance and the sum of its primary history follows. The House Report says, "These sections [§§ 208-221] contain provisions comparable to those in title I." (H.R. Rep. No. 2639, *supra*, at 30.) The Senate Report says no more. *See* S. Rep. No. 1775, *supra*, at 23. The invited cross-reference to the congruent jurisdictional provision, Section 44 of Title I, the Investment Company Act, reveals, in the full text of the House Report: "Contains the usual provisions regarding jurisdiction and venue of offenses and suits." (H.R. Rep. No. 2639, *supra*, at 26. *See also* S. Rep. No. 1775, *supra*, at 20.)

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port on Title II, which is in slightly greater detail than the Senate Report, is less than four printed pages in length. (H.R. Rep. No. 2639, 76th Cong., 3d Sess., 27-30 (1940)).

As with the relevant reports, a careful review of the House Hearings[32] and the Senate Hearings[33] also reveals nothing whatever about Section 214, nor was it discussed or debated on the floor of either house.[34] Absent some striking secondary evidence to the contrary, then, the scope, thrust and meaning of the relevant section of the Advisers Act must be gleaned from their text, in the light of the manifest purposes and the overall scheme of the statute, and in the context of accepted principles of substantive law.

Petitioners insist, however, that striking evidence of an intention to deny a private right of action at law is to be gleaned from secondary sources; such as statements of witnesses; subsequent congressional action or inaction on proposed amendments; the absence of specific private right provisions; and an inferential history of the text of Section 214. (*Brief for Petitioners* at 15-21.)

It is suggested that the declared regulatory purposes and provisions of the statute should be taken at less than face value because an SEC witness stated that the "basic approach" of Title II was to effect a "compulsory census" of the industry.[35] The witness did make that statement, early in the proceedings. Senate Hearings at 48. But this conciliatory approach was not even credited by the industry, once it had examined the bill—and it was surely not the approach or purpose of the enacted legisla-

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[32] Hearings on H.R. 10065 Before a Subcomm. of the House Comm. on Interstate and Foreign Commerce, 76th Cong., 3d Sess. (1940) [hereinafter "House Hearings"].

[33] Hearings on S. 3580 Before a Subcomm. of the Senate Comm. on Banking and Currency, 76th Cong., 3d Sess. (1940) [hereinafter "Senate Hearings"].

[34] For House floor discussion, see 86 Cong. Rec. 9807-19 (1940).

[35] (*Brief for Petitioners* at 15, 22.)

tion. Later, the vice president of the Investment Counsel Association of America, Inc., Douglas T. Johnston, appearing before the Senate committee, protested vigorously that the Advisers Act "is a far cry from the simple census proposed at that time." (Senate Hearings at 712.) He continued:

> "If a simple census can develop into a bill with the *broad regulatory provisions included in title II,* can one not be excused for wondering how the discretionary powers given in the bill would actually be used?" (*Id.*, emphasis added.)

Of course, the statements of witnesses are a relatively unreliable source of Congress' intent, especially if they conflict with the final reports to each house. *See American Airlines Inc.* v. *Civil Aeronautics Board,* 365 F.2d 939, 948 (D.C. Cir. 1966), and authorities cited therein; *see also Railroad Retirement Board* v. *Duquesne Warehouse Co.,* 149 F.2d 507, 510 (D.C. Cir. 1945), *aff'd,* 326 U.S. 446 (1946).

But Mr. Johnston was right. Whatever the importance of the information-gathering provisions of the Advisers Act, and whatever compromises were effected outside the record, both committees reported, and Congress passed, an act whose "essential purpose" was "to protect the public from . . . frauds and misrepresentations. . . ." (House Report No. 2639, *supra,* at 28.) No compromise affected the enactment of Section 206 or Section 215(b).

No more can an intent to deny implied private rights of action be derived from the absence of provisions explicitly creating private actions at law in the Advisers Act, as contrasted, *inter alia,* with the Investment Company Act. The argument was most recently rejected by this Court in *Cort* v. *Ash,* 422 U.S. 66, 82 n. 14. There, petitioners argued that Congress' provision of explicit private remedies in Title III of the Federal Election Campaign Act of 1971, and its failure to provide express civil remedies for violation of the criminal statutes amended by Title II of that Act, required the inference that Congress intended to exclude any private remedy arising out of the latter criminal statutes. Tersely, the Court rejected the contention, saying: "We find this excursion into extrapolation of legislative intent entirely unilluminating." (*Id.* at 82 n. 14.)

The same, and similar and even more sophisticated, arguments were utilized in connection with the implication of private rights of action under Section 10(b) of the 1934 Act, and Rule 10b-5. It was vigorously urged that the provision of explicit private rights of action in Sections 11 and 12 of the 1933 Act, as well as in Sections 9 and 16(b) of the 1934 Act, rendered the implication of private rights under Section 10(b) and Rule 10b-5 either anomalous or in conflict with congressional intention. *See generally* 3 Loss, *Securities Regulation* 1778-1792 (1961). Despite Professor Loss' fear that the perceived anomalies might cause judicial elimination of all implied private rights under that section and Rule, those arguments were rejected. *See, e.g., Fischman* v. *Raytheon Mfg. Co.,* 188 F.2d 783 (2d Cir. 1951).

The logic of petitioners' argument is more seriously flawed in this case because the Advisers Act plainly does provide for some private actions to redress violation of its regulatory provisions. Section 215(b) does permit the maintenance of a private action for equitable relief for such violations. Professor Loss has stated (referring to Section 29 of the 1934 Act) that the right granted by such a contract-avoidance provision is 'perhaps more express than implied." (3 Loss, *supra,* at p. 1759.) And there is no doubt but that Section 214 at least confers jurisdiction

over such actions. *See Abrahamson* v. *Fleschner,* 568 F.2d at 879, 882 n. 8 (Gurfein, J., dissenting).

Petitioners' strained effort to draw significance from Congress' amendment or non-amendment of the Advisers Act at various times between 1960 and 1977 is even less illuminating, there being no showing that Congress actually considered whether provision should be made for private actions in the Advisers Act, and actually decided to exclude them. This Court has uniformly held that, where a proposition has never been overtly considered, it cannot be deemed to have been either accepted or rejected. *Trailmobile Co.* v. *Whirls,* 331 U.S. 40 (1947); *Hust* v. *Moore-McCormack Lines,* 328 U.S. 707 (1946).

In 1960, Congress did indeed enact certain amendments to the Advisers Act. Pub. L. No. 86-750 (1960). But there is nothing in that enactment, nor in its legislative history, giving the slightest indication that Congress considered the issue of Commission enforcement *vis-a-vis* the desirability or undesirability of private enforcement—much less that it considered and concluded that only the SEC should enforce the Act. (*Compare, Brief for Petitioners* at 18.) The text and history of the 1960 amendments to the Advisers Act (Pub. L. No. 86-75 (1960)) show that the question of provision for private actions was never presented to Congress, let alone considered by it. The amendments, proposed to Congress by the SEC, were tailored specifically to respond to problems perceived by the Commission as hampering its enforcement efforts. H.R. Rep. No. 2179, 86th Cong., 2d Sess. 3 (1960); S. Rep. No. 1760, 86th Cong., 2d Sess. 2 (1960). Congress again focused on, and strengthened, the antifraud provision of the Act. It amended Section 206 to extend its coverage to unregistered investment advisers, and to empower the SEC to promulgate rules and regulations describing and proscribing fraudulent, manipulative and deceptive courses of conduct. Pub. L. No. 86-750, § 8, 9, 74 Stat. 885 (1960). To that extent, what Congress did in 1960 favors implication. What it did not do, and was not asked to do, and did not consider, is utterly valueless data.

The 1970 amendments to the Investment Company Act, and the accompanying amendments to the Advisers Act (Pub. L. No. 91-547 (1970), are immaterial. Once again, Congress never focused on the question whether the Advisers Act should, or already did, permit private actions, either at law or in equity. That Congress created a new private right of action under the Investment Company Act is in itself irrelevant. *See Cort* v. *Ash, supra,* 422 U.S. at 82 n. 14.

The overwhelming concern of Congress, in considering and enacting these amendments, was to remedy inadequacy in the regulation of the mutual fund segment of the securities industry that had been highlighted in the Wharton School Study of Mutual Funds, H.R. Rep. No. 2274, 87th Cong., 2d Sess. (1962). *See* S. Rep. No. 91-184, 91st Cong., 1st Sess., 1-3 (1969). In that particularized context, Congress considered and dealt with the problem of assuring effective redress where excessive and unjustified advisory fees had been paid by mutual funds to their advisers. This alone led to the enactment of Section 36(b) of the Investment Company Act. *See* 15 U.S.C. § 80a-35(b). Contrary to petitioners' claim, there was no consideration of the general question of "liability of investment advisers." [26] (S. Rep. No. 91-184, *supra,* at 5-7, 15-17; *see also* H.R. Rep. No. 91-1381, 91st Cong., 2d Sess., 12-13 (1970). The amendments to the Advisers Act were almost entirely to maintain consistency with provisions of the Investment Company Act; and the few exceptions have no bearing on

[26] *Brief for Petitioners* at 19.

the private actions issue. The descriptive text contained in the Senate Report, and cited by petitioners (*Brief for Petitioners* at 19), casts no light whatever upon the relevant purposes of the Advisers Act; and certainly in no way modifies the intentions expressed by the Congress that enacted that Act. *See, e.g., United States* v. *Southwestern Cable Co.*, 392 U.S. 157, 170 (1968), and authorities there cited.

With good reason, this Court has routinely rejected efforts to draw inferences from the inaction, or incomplete action, of Congress upon legislation introduced at the behest of an administrative agency, and there is no basis to change that rule to give any significance to the introduction of amendments to the Advisers Act in 1976 and 1977, or to Congress' inaction thereon. *United States* v. *Southwestern Cable Co., supra; Wong Yang Sung* v. *McGrath*, 393 U.S. 33 (1950).

The SEC and the cognizant Senate committee explicitly stated that the purpose of the proposed 1976 and 1977 amendments was to clarify, and not to change, the law relating to private actions under the Advisers Act. 1975-76 CCH Fed. Sec. L. Rep. ¶ 80,341 (Investment Advisers Act Release No. 491, Dec. 15, 1975); S. Rep. No. 94-910 94th Cong., 1st Sess., 8-9 (1976). There was, at the time, a split in the federal district courts on the question now before this Court; and the SEC desired to resolve the question, if possible, through legislation. (*Id.*) As Mr. Justice Harlan wrote, in *United States* v. *Southwestern Cable Co., supra*, ". . . administrative agencies should, in such circumstances, be encouraged to seek from Congress clarification of the pertinent statutory provisions." 392 U.S. at 170 (citations omitted).

In its report, the Senate committee stated its view that "[i]t is anomalous to deny advisory clients the right to

recover damages as a result of a violation of the Advisers Act when private rights of action in the same circumstances have been implied by the courts under other Federal securities laws." (S. Rep. No. 94-910, *supra*, at 8). The committee, however, voiced optimism, saying that it expected the courts would apply 'established legal principles" in deciding whether, and under what circumstances, an implied right of action should be recognized under the Advisers Act. (*Id.*, at 9.)

It is pointless to speculate whether the absence of further congressional action was due to satisfaction with developing judicial interpretation, the press of other, more urgent matters, or even inertia. The amendment was never approved or disapproved. Any sense of urgency, if it ever existed, may well have been vitiated by the soon-to-follow decisions in the *Abrahamson* case, the *Wilson* case and the case at bar. It is impossible to say; and impossible to say not. Like the record prior to the passage of the Advisers Act, the subsequent history only leads back to the statute itself, and its basic premises.

B. *The Advisers Act and Its Articulated Essential Purposes Sufficiently Indicate Congressional Intention to Allow Some Private Actions; and There Is Explicit Provision for Equitable Actions.*

At least implicit intention to allow some private actions for violation of Section 206 appears in the character of that section as such. It declares fraudulent, deceptive and, since 1960, manipulative conduct unlawful in order to protect an especial class of persons, thus meeting the first of the *Cort* v. *Ash* criteria. This alone is substantial evidence of an implicit legislative intent to permit appropriate remedies to be framed by the courts for enforcement of the right so created, *Fischman* v. *Raytheon Mfg. Co.*, 188 F.2d 783 (2d Cir. 1951); particularly where the pro-

priety of the implication of such rights was an accepted principle when the statute was enacted. *See e.g., Texas & Pacific Ry. Co.* v. *Rigsby, supra;* Restatement of Torts, *supra,* § 286. Such reasoning led to the proper acceptance of implied rights and remedies under Section 10(b) of the 1934 Act and Rule 10b-5; despite the fact that, as this Court has said, that "there is no indication that Congress, or the Commission . . . contemplated such a remedy . . . ." (*Ernst & Ernst* v. *Hochfelder,* 425 U.S. 185, 196 (1976).) It is every bit as valid here.

When Section 206 is read as it should be, in conjunction with Section 215(b), there is quite enough evidence of congressional intention to allow private relief sufficient to dispose of the case before this Court by affirmance of the ruling of the Court of Appeals. The latter provides that any contract "made in violation of any provision" of the Advisers Act, and any contract "the performance of which," or "continuance of any relationship or practice" under, involves violation of any provision of the Advisers Act, "shall be void." It is utterly indistinguishable from Section 29(b) of the 1934 Act, 15 U.S.C. § 78cc(b). The thrust of that section, and of Section 215(b), is that any contract so made or performed, and the continuation of any relationship unlawful thereunder, is "voidable at the option of the deceived party." *See Blue Chip Stamps* v. *Manor Drug Stores,* 421 U.S. 723, 736 (1975); citing *Deckert* v. *Independence Shares Corp.,* 311 U.S. 282 (1940). *See also, Goldstein* v. *Groesbeck,* 142 F.2d 422 (2d Cir. 1944). As this Court noted in *Blue Chip Stamps,* Section 29(b) of the 1934 Act was read, in the leading cases, as supporting the implication of a cause of action for damages under Section 10(b) of the 1934 Act and Rule 10b-5. *See Kardon* v. *National Gypsum Co.,* 69 F. Supp. 512, 514 (E.D. Pa. 1946); *Fischman* v. *Raytheon Mfg. Co.,* 188 F.2d 783, 787

n. 4 (2d Cir. 1951). Section 215(b) is of even greater significance in cases such as this, where a contract is central to the controversy. *See* 3 Loss, *op. cit., supra,* at 1759. *Accord, Abrahamson* v. *Fleschner,* 568 F.2d 862, 882 n. 8 (Gurfein, J., concurring and dissenting).

It is quite sufficient to dispose of the present case in respondent's favor that, unless Section 215(b) is to be nullified, a private right of action for equitable relief under the Advisers Act must be upheld; since only the injured party, and not the SEC, has the "option" to avoid a voidable agreement. *See, Mills* v. *Electric Auto-Lite Company,* 396 U.S. 375, 387-388 (1970), and authorities cited therein. Asserting the invalidity of the advisory agreement between TAMA and MTA, due to violation of, *inter alia,* Section 206, and attacking the transactions between MTA and TALC as well as the performance of TAMA's advisory function under that and other provisions, this action seeks a declaration that the investment advisory agreement was void; a decree avoiding that contract; restitution of the compensation received thereunder; and related relief with respect to the TALC-MTA transactions.

It is elementary that an action to avoid or rescind an agreement is "exclusively equitable in nature," *e.g., Ammerman* v. *Miller,* 488 F.2d 1285, 1295 (D.C. Cir. 1973); and that suit seeking rescission of a contract on account of fraud, and to recover the consideration paid thereunder, may be maintained in equity. *Deckert* v. *Independence Shares Corp., supra,* 311 U.S. at 289 and authorities cited therein. While money damages are also sought in the instant case, equitable jurisdiction remains; and with such jurisdiction the court should dispose of all claims, even if the only remedy found proper is an award of damages on the legal claims. *E.g., McGowan* v. *Parish,* 237 U.S. 285 (1915); *Kinney-Coastal Oil Co.* v. *Kieffer,* 277 U.S. 488

(1928); *Hartford Accident & Indemnity Co.* v. *Southern Pacific Co.*, 273 U.S. 207 (1927). *See also Mendez* v. *Bowie*, 118 F.2d 435, 440 (1st Cir.), *cert. denied*, 314 U.S. 639 (1941).

The leading cases arising under the federal securities laws hold that, where federally created rights are involved and there is thus federal jurisdiction over the controversy, the courts have whatever power is necessary to determine and apply appropriate remedies for violation of these rights. *E.g., J. I. Case Co.* v. *Borak*, 377 U.S. 426 (1964); *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375 (1970). *See also Sola Electric Co.* v. *Jefferson Electric Co.*, 317 U.S. 173 (1942). Surely then, even if the statute here at issue mandates dichotomous treatment of legal and equitable causes —itself an historical anomaly—there is no basis for denying implication of a private equitable action.

In *Abrahamson*, Judge Gurfein's dissent does not take issue with these principles, being explicitly restricted, on the facts of that case, to the question whether "a private action at law for damages should be implied" (at 879). That dissent was explicitly adopted by the dissenting judge in this case. Petitioners, having sought and obtained certiorari on the question whether *any* private right of action arises by implication under the Advisers Act, now restrict their argument to the claimed exclusion of actions at law for damages.[27] But that is not this case; and for this reason alone the decision of the Court of Appeals should be affirmed.

[27] This is manifest from their statement of the question presented, and permeates thereafter each argument advanced. (*E.g., Brief for Petitioners* at 2, 7, 11, 14, 21, 22, 32.) While so arguing, they do, without citation of authority, suggest that the arguments directed against actions for money damages support the conclusion that no private actions should be allowed. But, in the absence of reasoned explanation, and on a fair reading of their position, this suggestion cannot be seriously regarded.

Nonetheless, so as to deal with the entire question upon which certiorari was granted by this Court, we next consider whether an action that could be characterized as an action at law for damages may arise under the Advisers Act.

C. *Section 214 of the Advisers Act Does Not Exclude Jurisdiction Over an Action at Law for Damages Under the Act; Nor Does Its Language Manifest a Congressional Intent to Bar Private Actions.*

The absence of the phrase "actions at law" from Section 214 of the Advisers Act does not operate to exclude federal subject matter jurisdiction over such actions. The contrary is not seriously contended (*Brief for Petitioners*, 10); nor could it be. That subject matter jurisdiction, as such, existed was common ground between the majority and the dissent in *Abrahamson* v. *Fleschner, supra*, 568 F.2d at 875 n. 22 (majority opinion), 88 n. 5 (dissenting opinion). That there is general federal question jurisdiction over private claims arising by implication from federal positive law, constitutional or statutory, requires no exegesis here. *See, e.g., Bell* v. *Hood*, 327 U.S. 678 (1946); *Bivens* v. *Six Unknown Named Agents of the Federal Bureau of Narcotics*, 403 U.S. 388, 399 (1971) (concurring opinion per Harlan, J.); *Tunstall* v. *Brotherhood of Railway Firemen and Enginemen*, 323 U.S. 210 (1944). Thus, subject matter jurisdiction here also exists under 28 U.S.C. §1331 (1971). *See Brown* v. *Bullock*, 294 F.2d 415, 418 (2d Cir. 1961). In addition, there is respectable authority that the language in Section 214 granting to the federal district courts exclusive jurisdiction over "violations" of the Act is sufficient. *Bolger* v. *Laventhal, Krekstein, Horwath & Horwath*, 381 F. Supp. 260, 264 (S.D.N.Y. 1974); *Osborne* v. *Mallory*, 86 F. Supp. 869, 879 (S.D.N.Y. 1949). Once federal question jurisdiction was established, private rights of action have been

implied in the absence of any special or separate jurisdictional provisions in the relevant statute. *Abrahamson* v. *Fleschner, supra,* at 875 n. 22, citing *inter alia, Texas & Pacific Ry. Co.* v. *Rigsby, supra,* 241 U.S. at 39; *Odell* v. *Humble Oil and Refining Co.,* 201 F.2d 123, 126 (10th Cir.) *cert. denied* 345 U.S. 941 (1953).

Given the overwhelming consensus that private rights of action properly arise under the antifraud provisions of the other federal securities laws, the question, properly stated, is whether an exception should be made of Section 206 because the words "actions at law" are absent from Section 214. The Court in *Abrahamson* v. *Fleschner, supra,* concluded that:

> "There is not a shred of evidence in the legislative history of the Advisers Act to support the assertion that Congress intentionally omitted the reference to 'actions at law' in order to preclude private actions by investors." (568 F.2d at 875.)

The statement is entirely correct. The Congress never considered the language or its meaning; nor were its members ever given to believe that there was anything of moment to consider. When the Advisers Act was brought to the floor of the House, the accompanying committee report informed its members only that Section 214 was "comparable" to the jurisdictional provision of the companion Investment Company Act, Section 44. (H.R. Rep. 2639, 76th Cong., 3d Sess. 31 (1940).) Cross-reference yielded the information that Section 44 "[c]ontains the usual provisions regarding jurisdiction and venue of offenses and suits." (*Id.* at 26-27.) The Senate Report said, if possible, less. S. Rep. 1775, 76th Cong., 3d Sess. 20, 23 (1940).

Had the members of either house referred for enlightenment to the transcripts of the committee hearings, they would have found, in the House Hearings, the statement of SEC attorney David Schenker that "Section 214 covers jurisdiction of offenses and suits." [28] There is nothing else in those hearings, or in the more than 1,000 pages of the Senate Hearings, about Section 214. As to the congruent section of Title I, Schenker had told the House committee that "Sections 43, 44, 45 and 46 all pertain pretty much to well-established existing law." [29]

That is the sum, substance and totality of the legislative history of Section 214, as contained in the primary and most persuasive sources. The portions of the House and Senate Hearings cited in support of the argument that the omission of "actions at law" from Section 214 was intentional, do not even mention the point.[30]

The conclusion necessarily to be drawn is that, to the extent Congress or its committees actually considered the contents of Section 214, they had been given to believe, and had fairly assumed, that the effect of that provision was the same as the effect of all of the other, "usual" jurisdictional provisions of the securities laws.

Rather imaginatively, petitioners suggest, nonetheless, that there was a significant compromise which resulted in the conscious omission of the phrase "actions at law," in negotiations between the SEC and the industry over the text of the Advisers Act. (*Brief for Petitioners* at 8-9, 15-

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[28] House Hearings at 138.

[29] *Id.* at 37.

[30] *See* Senate Hearings at 712-713, 737-754, 1154, cited in *Brief for ICAA* at 3 nn. 3 & 5; House Hearings at 88-90, 92, cited in *Brief for ICAA* at 4 n. 4.

16.) The record is devoid of support for the claim. What does appear is that, at first, the Advisers Act was opposed, *in toto*, by numerous industry spokesmen; that compromises were effected; and that the final legislation had industry acquiescence. But all of this is irrelevant, since the areas of controversy and compromise were unrelated to the issues here. The testimony, in the 1940 House Hearings, of Dwight Rose, on behalf of the Investment Counsel Association of America (hereinafter, "ICAA"), summarizes the controversies, and their resolution.[31]

Neither his testimony, nor any other, supports petitioners' argument.

Petitioners, and the ICAA,[32] also resort to citation of a series of preliminary drafts of the legislation, offered without provenance, to support the claim of congressional intent to exclude actions at law. But such sources are value-

[31] "When the hearings were held on this bill before the Senate committee, the Association opposed it. We opposed it for three general reasons: First, in the original bill there was a confusion between investment counsel and investment trusts. We felt that the personal confidential relationship existing between the investment counsel and this client was so very different from the commodity of investment trust shares which investment trusts were engaged in selling, that any legislation to regulate these two different activities should be incorporated in separate acts. In the bill we felt that our clients were not properly protected in their confidential relationship. In the testimony before the Senate subcommittee there was quite a fight on that. It is not necessary to go into that here. Also we felt that powers given the Securities and Exchange Commission under the bill were unnecessarily broad and would lead to a great deal of uncertainty on the part of anyone who wished to practice his profession as to what might happen to him at any time.

"Following the hearings before the Senate subcommittee, we had conferences with the Securities and Exchange Commission, and all of our objections have been satisfactorily adjusted." House Hearings at 92.

[32] *Brief for ICAA, as Amicus Curiae, in Support of Petitioners* at 3-4.

less where, as here, the "committee changes relied upon were made without explanation." *Trailmobile Co.* v. *Whirls*, 331 U.S. 40 (1947). The Court there rightly declared that:

> "The interpretation of statutes cannot safely be made to rest upon mute intermediate legislative maneuvers." (*Id.*, at 61.)

A fortiori, these sources have no value when the changes, and their significance, were never made a part of the committee deliberations. *See Hust* v. *Moore-McCormack Lines*, 328 U.S. 707 (1946). They constitute no evidence that Congress had the question "presented to its attention," or that it chose one of the alternatives presented. *United States* v. *Pfitsch*, 256 U.S. 547, 552 (1921); *see also Wright* v. *Vinton Branch of Mountain Trust Bank*, 300 U.S. 440 (1937).

Even if the various drafts are considered, they fail to show that there ever was a proposed provision of the Advisers Act from which "actions at law" could have been deleted.[33] There is nothing to explain the changes, to indicate that they were discussed by the Senate or House com-

[33] The early versions of the Advisers Act contained a catchall provision, Section 208, which incorporated by reference more than a dozen sections of the concurrent draft of the Investment Company Act. (*Brief for ICAA, supra*, at 3-4, and Exhibits B, C.) The Investment Company Act jurisdiction section thus incorporated (Section 40(a)) in turn incorporated by reference Section 25 of the Public Utility Holding Company Act of 1935. (*Brief of ICAA, supra*, Exhibits B, C.) The Advisers Act was changed first. A committee print of S. 3580, dated May 24, 1940, includes a new section (then Section 213), specifically dealing with jurisdiction, in substantially the language finally enacted as Section 214. (*Brief of ICAA, supra*, Exhibit C, at A19-20.) No separate jurisdictional section appeared in a draft of the Investment Company Act until, in a committee print of June 4, 1940, the first draft of Section 44 of that title was inserted. (*Brief for ICAA, supra*, Exhibit C, at A25.)

mittees or even to identify the draftsman. All that is really clear is that they were not deemed worth mention. This is the best guide to their proper treatment now.

The absence of the phrase "actions at law" from Section 214 is, on the state of the record, more than adequately explained in *Abrahamson* v. *Fleschner, supra,* 568 F.2d at 874-875. The draftsman provided, in Section 214, for special federal question jurisdiction over only those suits expressly authorized by the Advisers Act. The draftsmen of Section 44 of the Investment Company Act (15 U.S.C. § 80a-43), of Section 22 of the 1933 Act (15 U.S.C. § 77v) and of Section 27 of the 1934 Act (15 U.S.C. § 78aa), in specifying jurisdiction in the district courts over "all suits in equity and actions at law," had done the same. This was necessary to assure such jurisdiction over private civil actions expressly created by those statutes, without reference to the jurisdictional amount, or any other, limiting provision of the general federal question jurisdiction statute, 28 U.S.C. § 1331. It is argued that this explanation is erroneous, and that the express civil liability sections of the earlier acts already conferred such jurisdiction. But the rights-creating provisions of the earlier acts typically provide, as in the case of Section 11 of the 1933 Act, 15 U.S.C. § 77k, only that suit may be brought "in any court of competent jurisdiction . . . ." This language confers no jurisdiction on any particular court; unless another statute establishes that such court *is* one of "competent jurisdiction." Thus, the entirely sensible explanation of the *Abrahamson* majority remains unrebutted.

The necessary conclusion, we submit, is that Section 214 of the Advisers Act has no legislative history worthy of the name. In the absence of any considered determination by either house of Congress as such, or by either cognizant committee of Congress; and in the absence of any testimony

directed to the point even in the hearings before these committees, we submit that whatever thoughts may be ascribed to an unidentified draftsman, never reviewed by those with the power to enact, they are nothing on which to base the argument that the language of Section 214 either excludes, or indicates any congressional intention to exclude, private actions under the Advisers Act.

In this case, then, the answer to the second question posed by *Cort* v. *Ash,* 422 U.S. 66 (1975), is that there are implicit indicia from the regulatory aspects of the statute, in light of Congress' specific statements of its purpose, favoring implication of private remedies. Nothing in the legislative history negates this, or illuminates congressional intention. There is explicit indication that equitable relief is available under Section 215(b), in respect of voidable agreements; and Section 214 does not justify denial of appropriate federal remedies for violation of the Act.

V.

It Is Wholly Consistent With the Underlying Purposes of the Legislative Scheme to Recognize Implied Private Remedies for Violation of Section 206 of the Advisers Act.

The third of the considerations in *Cort* v. *Ash,* 422 U.S. 66, 78, is whether recognition of an implied right of action is consistent with the underlying legislative purposes of the legislative scheme; that is, whether allowance of the remedies sought would further the achievement of the "primary congressional goal." (*Id.,* at 82.)

The broad purposes of the Advisers Act were summarized in *Securities and Exchange Commission* v. *Capital Gains Research Bureau,* 375 U.S. 180, 186:

"The Investment Advisers Act of 1940 was the last in a series of Acts designed to eliminate certain abuses in the securities industry, abuses which were found to have contributed to the stock market crash of 1929 and the depression of the 1930's. It was preceded by the Securities Act of 1933, the Securities Exchange Act of 1934, the Public Utility Holding Company Act of 1935, the Trust Indenture Act of 1939, and the Investment Company Act of 1940. A fundamental purpose, common to these statutes, was to substitute a philosophy of full disclosure for the philosophy of *caveat emptor* and thus to achieve a high standard of business ethics in the securities industry." (Footnotes omitted.)

As discussed in Point III, *supra*, the particularized fundamental purpose of the Advisers Act is tersely and bluntly set forth in the reports of the cognizant congressional committees. The House Report declares that:

"The *essential purpose* of title II of the bill is *to protect the public from the frauds and misrepresentations of unscrupulous* tipsters and touts and to safeguard the honest investment adviser against the stigma of the activities of these individuals *by making fraudulent practices by investment advisers unlawful.*" (H.R. Rep. 2639, 76th Cong., 3d Sess., 28 (1940); emphasis added.)

The Senate Report is equally blunt, contains the same language concerning public protection from "frauds and misrepresentations" and emphasizes that:

"The report of the Commission to the Congress and the record before the committee is clear that the solution of the problems and abuses of investment advisory services—individuals and companies which either handle pools of liquid funds of the public or give advice with respect to securities transactions—cannot be effected without federal legislation." (S. Rep. 1775, 76th Cong., 3d Sess., 21 (1940).)

This is the articulated fundamental purpose, embodied not only in the Reports, but in Section 206 and Section 215(b). Whether equitable or legal in nature, these rights cannot be inconsistent with—that is, in conflict with—that fundamental purpose.

Petitioners refuse to meet the issue. Instead, they revive the pointless argument that, despite the anti-fraud, and contract-avoiding sections of the Advisers Act, it is no more than a "compulsory census." This has been dealt wtih. (*See* Point IV-A, *supra.*) No more pertinent is the assertion that the limits placed upon the SEC power to generate publicity for its investigations by Section 210 of the Advisers Act have any bearing on the propriety of implied remedies. Section 210 was a specific response to the protestations of industry spokesmen that the mere announcement of an SEC investigation would ruin an adviser; as would the threat that client confidentiality might be unfairly invaded.[34] The fear was recognized as rational in the economic climate of 1940. The limitation is itself narrow. It is grasping at straws to suggest that it manifests an intent to protect advisers from their clients. *Cf. Piper* v. *Chris-Craft Industries, Inc.*, 430 U.S. 1 (1977).

No distinction between "goals" and "means" (*Brief for Petitioners* at 23-24) can turn aside the force of the point that the implication of a private right of action is entirely consistent with the statutory purpose to render fraud unlawful; only petitioners' own inaccurate footnote suggests that "negligent" investment advisers would be subject to

[34] *See* Senate Hearings, 718-723; S. Rep. No. 1775, 76th Cong., 3d Sess., 23 (1940).

such actions (*id.*, at n. 32; see p. 59, *infra*), and there is no authority for the entire *non sequitur*. *Compare S. Rep.* No. 1760, 86th Cong., 2d Sess. 2 (1960).

The cases holding that implication of private rights of action was inconsistent with an underlying legislative scheme demonstrate the interdependence among the several *Cort* v. *Ash* criteria. The conclusion that no federal right in favor of plaintiffs had been created, and that Congress had not intended to do so, was determinative of this third criterion in *Piper* v. *Chris-Craft Industries, Inc., supra;* and *Cort* v. *Ash, supra.* The determination that permission of a private action would interfere with the operations of, and the proper exercise of discretion by, the agency given primary jurisdiction to deal with the problems that brought forth the legislation, was controlling in *Securities Investor Protection Corp.* v. *Barbour,* 421 U.S. 412 (1975), and *National Railroad Passengers Corp.* v. *National Ass'n of Railroad Passengers,* 414 U.S. 453 (1974). Congress had manifested a specific intent to deny private actions by creating administrative machinery to decide the matters on which court adjudication were sought, and, in the last-cited case, by publicly determining to delete a specific private action provision. Such cases have not the remotest relevance to the case at bar, as was made plain in *Cort* v. *Ash* itself, 422 U.S. at 82 n. 14.

Conversely, allowance of some private actions under the Advisers Act is necessary, in fact, to avoid a clear inconsistency, nullification of Section 215(b). As previously discussed, that statute gives the right of avoidance to the injured party alone (*see Deckert* v. *Independence Shares Corp.*, 311 U.S. 282 (1940)), and failure to allow a private action would nullify it. *See Kardon* v. *National Gypsum Co.*, 69 F. Supp. 512 (E.D. Pa. 1946).

Recognizing the weakness of their suggestion of inconsistency, petitioners shift ground and argue that this Court must find an implied remedy necessary, or deny it. No case so held, after finding that the statute created a federal right in favor of a plaintiff. *Piper* v. *Chris-Craft Industries, Inc., supra,* whence petitioners select this formulation, does not so phrase the criterion; but rather frames it in the language of *Cort* v. *Ash, supra.* It uses the concept of necessity as a term of conclusion, expressing the result of consideration of the questions posed.

Further, in the sense in which the term is used in *J. I. Case Co.* v. *Borak, supra,* implication of a private right of action under Section 206 is a necessary supplement to Commission enforcement. Here, as there, it is clear that the SEC alone cannot effectively enforce the statute. In *Borak,* the Court highlighted the SEC's inability to monitor in timely fashion the approximately 2,000 proxy solicitations that it received each year. Still less is it equipped to review the contracts and activities of all registered and exempt or unregistered investment advisers. Between 1969 and 1975, the number of registered investment advisers more than doubled, from 1,343 to 3,606. S. Rep. No. 94-910, 2 (1976). That growth alone has raised "serious questions" as to the adequacy of the existing mechanisms for enforcement of the Advisers Act. (*Id.*)

As the SEC itself has pointed out, it is not even able to keep informed about the activities of the investment advisers it is supposed to regulate, because investment advisers are not required to file periodic or other reports. (SEC Institutional Investor Study Report, H. Doc. No. 92-64, Part 2, 92d Cong., 1st Sess., at 360 (1971).)

The naked existence of statutory provisions authorizing the Commission to regulate investment advisers so as to prevent, or punish, fraud and like misconduct is meaning-

less. There has not been, and cannot be, any demonstration that the Commission is able effectively to enforce the anti-fraud provision of the Advisers Act.

It follows that consistency with the underlying legislative scheme results from, and even depends on, recognition of private rights of action under the Advisers Act.

VI.

The Federal Courts Should Entertain the Actions That Are Brought to Vindicate Private Federal Rights Arising Under the Advisers Act.

The answer to the fourth question posed by *Cort* v. *Ash, supra,* is, on authority and sound reason, dictated by the answer to the first. In the securities law context, as elsewhere, this Court has declared the law to be that the vindication of federally created rights, and the manner of that vindication, are the business and duty of the federal courts. *J. I. Case* v. *Borak,* 377 U.S. 426 (1964); *Sola Electric Co.* v. *Jefferson Electric Co.,* 317 U.S. 173 (1942); *Textile Workers Union* v. *Lincoln Mills,* 353 U.S. 448 (1957). The contrary result has been reached where, and only where, it has been determined that no federal right in plaintiff's favor had been created. *See Cort* v. *Ash, supra; Piper* v. *Chris-Craft Industries Inc.,* 430 U.S. 1 (1977).

It is no answer to argue, as do petitioners, that claims for violation of Section 206 of the Advisers Act should be relegated to the state courts because they can be restated in the terminology of traditional common law causes of action, *i.e.,* fraud, misrepresentation or, as a catchall, breach of fiduciary duty. Because federal law is built upon the framework of common law jurisprudence, there are few, if any, claims for relief that could not be so restated,

with a modicum of semantic imagination. The existence of such available analogies has not prevented the federal courts from recognizing and implying appropriate federal private rights, whether under the securities laws, in the law of trespass or with respect to torts arising out of violation of federal constitutional rights. *See, e.g., Deckert* v. *Independence Shares Co. Inc., supra; Fischman* v. *Raytheon Mfg. Co., supra; Wyandotte Transportation Co.* v. *United States,* 389 U.S. 191 (1967); *Bivens* v. *Six Unknown Named Agents of the Federal Bureau of Narcotics,* 403 U.S. 388 (1971). It has recently been noted, in *Butz* v. *Economou,* —— U.S. ——, 98 S. Ct. 2894, 2919 (1978) (Rehnquist, J., dissenting), that there is a close correspondence between claims asserted to arise directly under the Constitution and claims describable in terms of the common law.

It is axiomatic that the concepts of fraud inhering in the securities laws, including the 1934 Act and the Advisers Act, were built upon the common law concepts typically embodied in the traditional tort of deceit. 3 Loss, *Securities Regulation* 1430-1444 (1961). But, as Professor Loss there said, "The fact is that the courts have repeatedly said that the fraud provisions in the SEC acts . . . are not limited to circumstances which would give rise to a common law action for deceit." (*Id.,* at 1435.)

To hold otherwise would be to say that "Congress had no purpose in enacting regulatory statutes in this field and that its legislation in the field is meaningless." *Norris & Hirshberg* v. *Securities and Exchange Commission,* 177 F.2d 228, 233 (D.C. Cir. 1949). The federal courts have recognized that state law rights and remedies had proved inadequate to protect the rights of investors in transactions and relationships within the ambit of the federal securities laws. *Securities and Exchange Commission* v. *Capital*

Gains Research Bureau, 375 U.S. 180, 186 (1964); *Fischman* v. *Raytheon Mfg. Co., supra.*

Beyond the question of adequacy of common law forms of action, it is as true in the field of securities law regulation as in other fields of primary federal concern that the substantive content of the rights and remedies provided should be uniform throughout the country. To permit varying doctrines of state law, substantive or procedural, to affect adversely the application of federal regulatory law, would be an impermissible interference with its effectiveness. As this Court held in *Sola Electric Co.* v. *Jefferson Electric Co., supra,* the legal relations arising under such laws "must be deemed governed by federal law having its source in those statutes, rather than by local law." (317 U.S. at 176; citations omitted.)

A cause of action arising under a federal statute that is part of the body of law providing for national regulation of the securities industry is neither a traditional state law claim nor one in an area of basic state concern. Federal law is the appropriate law, and the federal courts are the proper forum.

VII.

Every Valid Policy Consideration That May Bear on This Case Supports Recognition of an Implied Right of Action Under the Advisers Act.

The Court of Appeals held in this case that a private right of action for injunctive relief and damages could be implied under the Advisers Act in favor of an appropriate plaintiff. The correctness of that holding is all that is before this Court. It warrants affirmance.

The interpretation, construction and enforcement of federal statutory law is, next to the interpretation, application and protection of the Constitution itself, the quintessential business of the federal courts. This should not need to be said; but the essence of petitioners' final plea for reversal of the Court of Appeals is that this and all similar cases should be barred from the federal courts; lest the courts be burdened with the task of applying and interpreting the statute, and setting the legal perimeters of such cases. (*Brief for Petitioners* at 28-29.)

It is difficult to conclude that any considerations of legal or practical policy justify, much less mandate, so gross a departure from the spirit expressed in the *Borak* case, where a unanimous Court agreed that it was "the duty of the courts to be alert," to effectuate the purposes of federal positive law, and to make meaningful the rights arising under that law. (377 U.S. at 433.)

There is nothing here to justify departure from these standards, or transgressing any limitations on private actions established by this Court. The threats to existing limitations on securities law actions; the danger of unlimited, open-ended suits; and the panoply of related

demons conjured by petitioners, are offered as an appeal to unreason.

In *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185 (1976), this Court held that *scienter* was a necessary element of an action arising under Section 10(b) and Rule 10b-5. In so doing, it thus made applicable in all of the federal courts the existing rule in the Second Circuit. *See, e.g., Lanza* v. *Drexel & Co.*, 479 F.2d 1277 (2d Cir. 1973). Because the type of conduct prohibited by Section 206 of the Advisers Act is indistinguishable in this regard from that prohibited by Rule 10b-5, it is fair to presume that the federal courts (in giving proper scope to Section 206 actions) will be appropriately guided. Affirmance here does not erode, and will not cause other courts to erode, the holding in *Ernst & Ernst.*

The rest of petitioners' practical or policy arguments have still less bearing on this case. They constitute a recital of imagined perils growing out of the factual situation said to be presented in *Abrahamson*, in which this Court denied certiorari (436 U.S. 913 (1978)). The case at bar, since it arises out of the making and performance of an investment advisory agreement and transactions integrally related to the relationship between MTA, its adviser and its adviser's parent and affiliate, is a peculiar context in which to relitigate *Abrahamson.* In any event, the imagined perils are nonexistent in the Advisers Act context.

In *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723 (1975), this Court confirmed the "purchaser-seller" requirement as an essential element in actions brought under Section 10(b) of the 1934 Act and Rule 10b-5. Again, this was the law in the Second Circuit, *Birnbaum* v. *Newport Steel Co.*, 193 F.2d 461 (2d Cir. 1952), *cert. denied*, 343 U.S. 956 (1952), and the majority rule. *See generally,*

Jacobs, The Impact of Rule 10b-5, § 38.01 (1978 ed.). No such requirement should or can be superimposed on Section 206, which deals with the adviser-client relationship, and is not specifically directed toward purchase or sale transactions. But actions grounded in Section 206 have their own inherent limits, as defined by the bounds of the relationship they arise from.

In the *Blue Chip Stamps* case, the Court expressed concern that, but for the "purchaser-seller" requirement, an unlimited universe of putative plaintiffs who, having had no transactional or other relationship with putative defendants, would nonetheless would be able to maintain actions on the theory that they had refrained from entering into transactions because of representations or omissions chargeable to such defendants. Such claims might be unreasonably difficult to defend and expose defendants to unjustifiable risk. (421 U.S. at 754-755.)

That problem is neither presented nor suggested by the case at bar, or like cases. Only the known, limited class of persons who can assert claims in connection with the making or performance of an advisory contract, or a course of conduct in an advisory relationship, are eligible to sue under the terms of Section 206 of the Advisers Act. Petitioners are not faced with the problem of disproving "what a plaintiff says he would have done." *See Abrahamson* v. *Fleschner, supra*, 568 F.2d at 884 (Gurfein, J., concurring and dissenting). Outside of the precise context of *Blue Chip*, the fear is, in any event, lacking in reality. In those cases where a plaintiff's actual state of mind is part of his case, the defendant does not have to "disprove" it. This is elementary. If what is actually being expressed is a fear of the competence of triers of the facts, no evidence is offered for its validity. If the point is that some questions cannot be left to the unguided determination of such

triers, the courts have, without great difficulty, established guiding principles. *See TSC Industries* v. *Northway, Inc.*, 426 U.S. 438 (1976).

Eventually, petitioners fall back upon a series of unfounded assertions, with respect to the merit or lack of merit of other cases not before this Court. *Brief for Petitioners,* 30-31.) They offer the odd proposition that, since certain suits have been brought against investment advisers to real estate trusts, since a number of these have been settled, and since some have been dismissed or withdrawn, it follows that the settled cases were so terminated, for more than was warranted on their merits, due to defendants' amorphous fears. This chain of suppositious innuendo is said to constitute reason for reversal here. Quite the contrary. It should be disregarded because it is based upon asserted facts not of record, unverified and incapable of verification. The subjective and biased interpretation of the asserted data is supported by neither authority nor expertise. Lastly, as is so often the case, the only verifiable datum offered—that is, the only reported decision mentioned—is wrongly described and miscited.[35] The formulary protestations of corporate defendants are not data; nor are they a basis for making, or finding, correct rules of law.

As petitioners' argument draws to a close, its underlying theme is clarified. They ask this Court to disregard the

[35] That reported case, *Jones* v. *Equitable Life Assurance Society,* 409 F. Supp. 370 (S.D.N.Y. 1975), offered as an example of a settled case and, by innuendo, an unjustified settlement, was decided for defendants. (*Compare Brief for Petitioners,* 30 n. 54.) The case cited as *Cooper* v. *USF Investors,* U.S.D.C., S.D.N.Y., 73 Civ. 2769 (MP), is misleadingly described. Reference to the cited file shows that, under the title *Independence Mortgage Trust* v. *USF Investors Inc.*, that case was settled, after the trust, by its new board of trustees, had been consensually substituted as plaintiff, and after the bankruptcy of the advisory company's parent.

actualities of the case at bar and to abandon the age-old rule that it will decide only the case or controversy that is actually before it. Petitioners' thesis is that suits brought by private plaintiffs under the federal securities laws should be presumed unmeritorious, and an imposition; that the federal courts should find ways to deny access to the courts to such investors; and that this is more important than adherence to the orderly process of deciding litigation on the law and on the merits. Petitioners look with feigned horror on the prospect that courts may be called upon in the future to determine litigation testing the "meaning, application and outer limits" of the Advisers Act. (Brief for Petitioners, 32). How much wiser it would be, they say, to rule that, so far as the community of investors is concerned, the Act has no meaning, no application and no rights to limit.

The Court of Appeals here, and the courts that decided *Abrahamson* and *Wilson,* have by their acts already answered this appeal. They have carefully and precisely applied the law as expounded by this Court; and they have not found themselves burdened or oppressed by the need to adjudicate the claims presented.

Little more than fifteen years ago, in *Securities and Exchange Commission* v. *Capital Gains Research Bureau Inc.,* 375 U.S. 180 (1963), this Court manifested its understanding that federal regulation of the securities industry, at a level of stringency sufficient to create confidence in the integrity of the capital market, was an essential ingredient to the economic well-being of the nation. That is as true now as it was then.

The rights recognized by the courts below, and their enforcement in appropriate cases, will contribute to that goal.

CONCLUSION

Recognition of an implied right of action under the Advisers Act, whether equitable or legal in character, is appropriate and correct; is a continuance and confirmation of sound and tested principles of judicial decision; and follows from a correct analysis of each and all of the criteria established by this Court.

Respondent respectfully prays for an order of this Court affirming the decision and order of the Court of Appeals for the Ninth Circuit.

Respectfully submitted,

ERIC L. KEISMAN
Attorney for Respondent
845 Third Avenue
New York, New York 10022
Telephone: (212) 759-4600

Of Counsel:

PHILIP JONES
MARIAN R. PROBST
SAMUEL R. DOLGOW
WOLF POPPER ROSS WOLF & JONES

ADDENDUM

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Section 206, Investment Advisers Act of 1940; 54 Stat. 852, as amended, 4 Stat. 887, 15 U.S.C. § 80b-6:

§ 80b-6. Prohibited transactions by investment advisers.

It shall be unlawful for any investment adviser, by use of the mails or any means or instrumentality of interstate commerce, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud any client or prospective client;

(2) to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client;

(3) acting as principal for his own account, knowingly to sell any security to or purchase any security from a client, or acting as broker for a person other than such client, knowingly to effect any sale or purchase of any security for the account of such client, without disclosing to such client in writing before the completion of such transaction the capacity in which he is acting and obtaining the consent of the client to such transacton. The prohibitions of this paragraph shall not apply to any transaction with a customer of a broker or dealer if such broker or dealer is not acting as an investment adviser in relation to such transaction;

(4) to engage in any act, practice, or course of business which is fraudulent, deceptive, or manipulative. The Commission shall, for the purposes of this paragraph (4) by rules and regulatons define, and pre-

scribe means reasonably designed to prevent, such acts, practices, and courses of business as are fraudulent, deceptive, or manipulative.

Aug. 22, 1940, c. 686, Title II, § 206, 54 Stat. 852; Sept. 13, 1960, Pub.L. 86-750, §§ 8, 9, 74 Stat. 887.

Section 214, Investment Advisers Act of 1940; 54 Stat. 856, 15 U.S.C. § 80b-14:

§ 80b-14. Jurisdiction of offenses and suits.

The district courts of the United States and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have jurisdiction of violations of this subchapter or the rules, regulations, or orders thereunder, and, concurrently with State and Territorial courts, of all suits in equity to enjoin any violation of this subchapter or the rules, regulations, or orders thereunder. Any criminal proceeding may be brought in the district wherein any act or transaction constituting the violation occurred. Any suit or action to enjoin any violation of this subchapter or rules, regulations, or orders thereunder, may be brought in any such district or in the district wherein the defendant is an inhabitant or transacts business, and process in such cases may be served in any district of which the defendant is an inhabitant or transacts business or wherever the defendant may be found. Judgments and decrees so rendered shall be subject to review as provided in sections 225 and 347 of Title 28, and section 7, as amended, of the Act entitled "An Act to establish a court of appeals for the District of Columbia", approved February 9, 1893. No costs shall be assessed for or against the

Commission in any proceeding under this subchapter brought by or against the Commission in any court.

Aug. 22, 1940, c. 686, Title II, § 214, 54 Stat. 856.

Section 215, Investment Advisers Act of 1940; 54 Stat. 856, 15 U.S.C. § 80b-15.

§ 80b-15. Validity of contracts

(a) Any condition, stipulation, or provision binding any person to waive compliance with any provision of this subchapter or with any rule, regulation, or order thereunder shall be void.

(b) Every contract made in violation of any provision of this subchapter and every contract heretofore or hereafter made, the performance of which involves the violation of, or the continuance of any relationship or practice in violation of any provision of this subchapter, or any rule, regulation, or order thereunder, shall be void (1) as regards the rights of any person who, in violation of any such provision, rule, regulation, or order, shall have made or engaged in the performance of any such contract, and (2) as regards the rights of any person who, not being a party to such contract, shall have acquired any right thereunder with actual knowledge of the facts by reason of which the making or performance of such contract was in violation of any such provision.

Aug. 22, 1940, c. 686, Title II, § 215, 54 Stat. 856.